

Take 5

for business

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Participating in
digital banking,
Malaysia

EY

Building a better
working world

Industry 4.0

has spurred numerous **technology-based innovations** that have accelerated the **transformation** of business models, global market access, governance and regulatory frameworks.

In a series of measures aimed at enabling **innovative application of technology** in Malaysia's financial sector, Bank Negara Malaysia (BNM) has recently released the **Policy Document on Licensing Framework for Digital Banks**.

The Framework seeks innovative business models to serve Malaysia's **underserved and unserved** market segments. To apply for a digital banking license, **traditional, licensed banks** (including Islamic banks) and **new participants** can submit their applications to BNM no later than 30 June 2021.

“

As we step into a new decade, the introduction of **digital banks** will strengthen the growth of Malaysia's digital platform economy, expand market access, **optimize business performance** and delight netizens.

Chow Sang Hoe

EY Asean Consulting Leader
Malaysia Consulting Managing Partner
Ernst & Young Advisory Services Sdn Bhd

The microcosm of a digital bank

Digital banks are not merely a digital channel for banking. They are fundamentally different to a bank with digital channels.

True digital players embed “digital” in all aspects – business model, operating model, technology and talent.



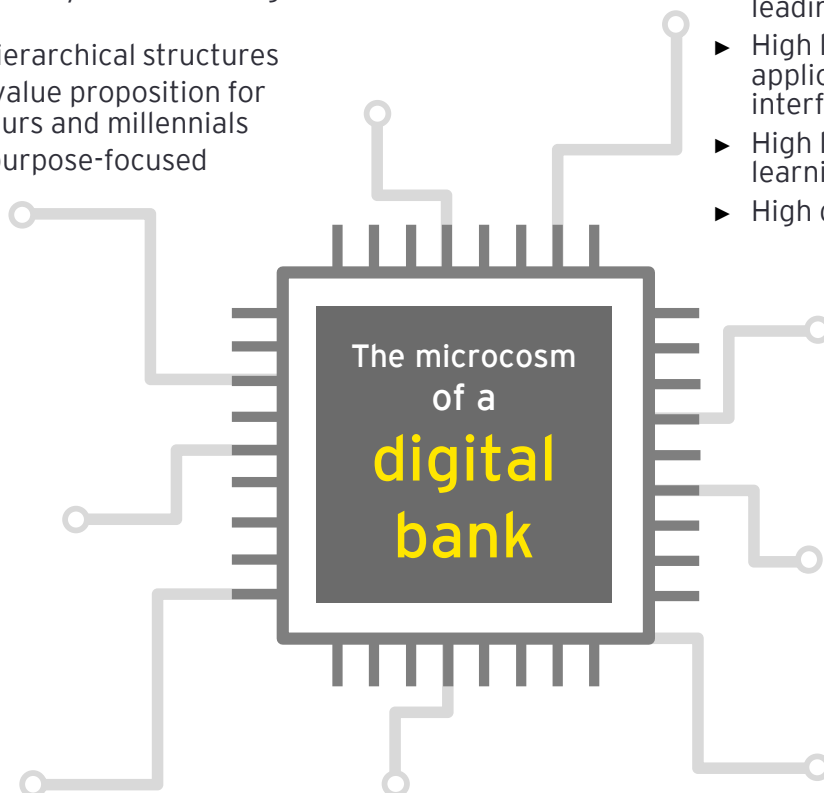
Talent

- ▶ High proportion of engineers and design professionals
- ▶ Multi-disciplinary teams working together
- ▶ Flat, non-hierarchical structures
- ▶ Employee value proposition for entrepreneurs and millennials
- ▶ Values or purpose-focused



Technology

- ▶ Configurable core banking
- ▶ Built on today's technology leading practices
- ▶ High leverage of cloud and open application programming interfaces (APIs)
- ▶ High leverage of AI and machine learning
- ▶ High degree of automation



Business model

- ▶ Target micro-segments
- ▶ World-class Customer Experience (CX)
- ▶ Simple products, pricing and transparency
- ▶ High degree of personalization
- ▶ Embed in daily life of target segments



Operations

- ▶ No or limited branch network
- ▶ Design process for no operations (NoOps)
- ▶ Aim to achieve low cost to income ratio (CIR)
- ▶ Mobile-only, virtual or robo-led servicing
- ▶ Leverage non-traditional data for credit assessment

Sources:

- ▶ EY Consulting
- ▶ Other relevant sources

Accelerating digital transformation

Digital banking to drive financial inclusion

Bank Negara Malaysia (BNM)'s Policy Document on Licensing Framework for Digital Banks aims to drive financial inclusion and deliver quality and responsible usage of financial services.

Up to five licenses may be issued to qualified applicants to establish digital banks to conduct either a conventional or Islamic banking business. The licenses will be granted by Q1 2022.

Digital banks: 5 application criteria

1

Best interest of Malaysia

Commitment to driving financial inclusion, including ensuring quality access and responsible usage of financial services

2

Demonstrate viability and sound operations

Maintain asset threshold of no more than RM3b in the first 3-5 years ("Foundational" phase)

3

Comply with regulations

Must comply with Financial Services Act (FSA) and Islamic Financial Services Act (IFSA) regulations, with simplified regulatory requirements in the "Foundational" phase

4

Meet the needs of the underserved and unserved segments

Offer meaningful access and responsible, affordable financial solutions

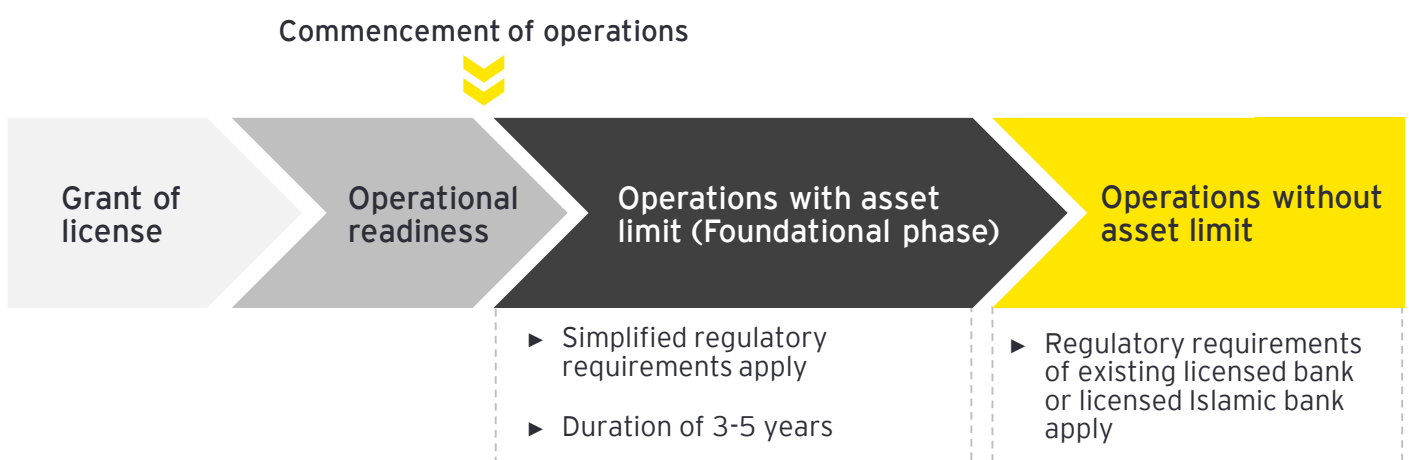
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Safeguard the integrity and stability of the financial system

Through capital funds of RM100m in the "Foundational" phase, and RM300m thereafter

Operational timeline for digital banks

The timeline for the operational progression and associated regulatory requirements of a licensed digital bank is shown below:



Sources:
▶ Licensing Framework for Digital Banks, Bank Negara Malaysia
▶ Press releases, Bank Negara Malaysia

Regulatory requirements during Foundational phase

Licensed digital banks must comply with the equivalent regulatory requirements applicable to a licensed bank or Islamic bank, except where specified below:

	Areas of simplification or exemption to the existing regulatory framework
Capital adequacy requirements	<ul style="list-style-type: none"> ▶ Minimum Total Capital Ratio (TCR) of 8% with simplified requirements of the following: <ul style="list-style-type: none"> ▶ <u>Capital components</u> <ul style="list-style-type: none"> ▶ Only Common Equity Tier 1 (CET1) capital is recognized as eligible regulatory capital ▶ Exempted from capital buffer requirements ▶ <u>Risk-weighted assets</u> <ul style="list-style-type: none"> ▶ Simplified requirements for credit risk, operational risk and market risk ▶ Exempted from the large exposure risk requirement (LERR)
Liquidity	<ul style="list-style-type: none"> ▶ Hold an adequate stock of unencumbered Level 1 and Level 2A high-quality liquid assets (HQLA) equivalent to at least 25% of its total on-balance sheet liabilities
Stress testing	<ul style="list-style-type: none"> ▶ Exempted
Public disclosures	<ul style="list-style-type: none"> ▶ Simplified requirements
Shariah governance	<ul style="list-style-type: none"> ▶ Simplified requirements

Considerations for assessing shareholders

BNM considers the ability of applicants and relevant shareholders to contribute to a proposed licensed digital bank in the following areas:



Sources:
 ▶ Licensing Framework for Digital Banks, Bank Negara Malaysia

Considerations for digital banking

6 capabilities to run a digital bank

Consortiums or partnerships can be formed to develop the critical capabilities needed to successfully launch a digital bank.

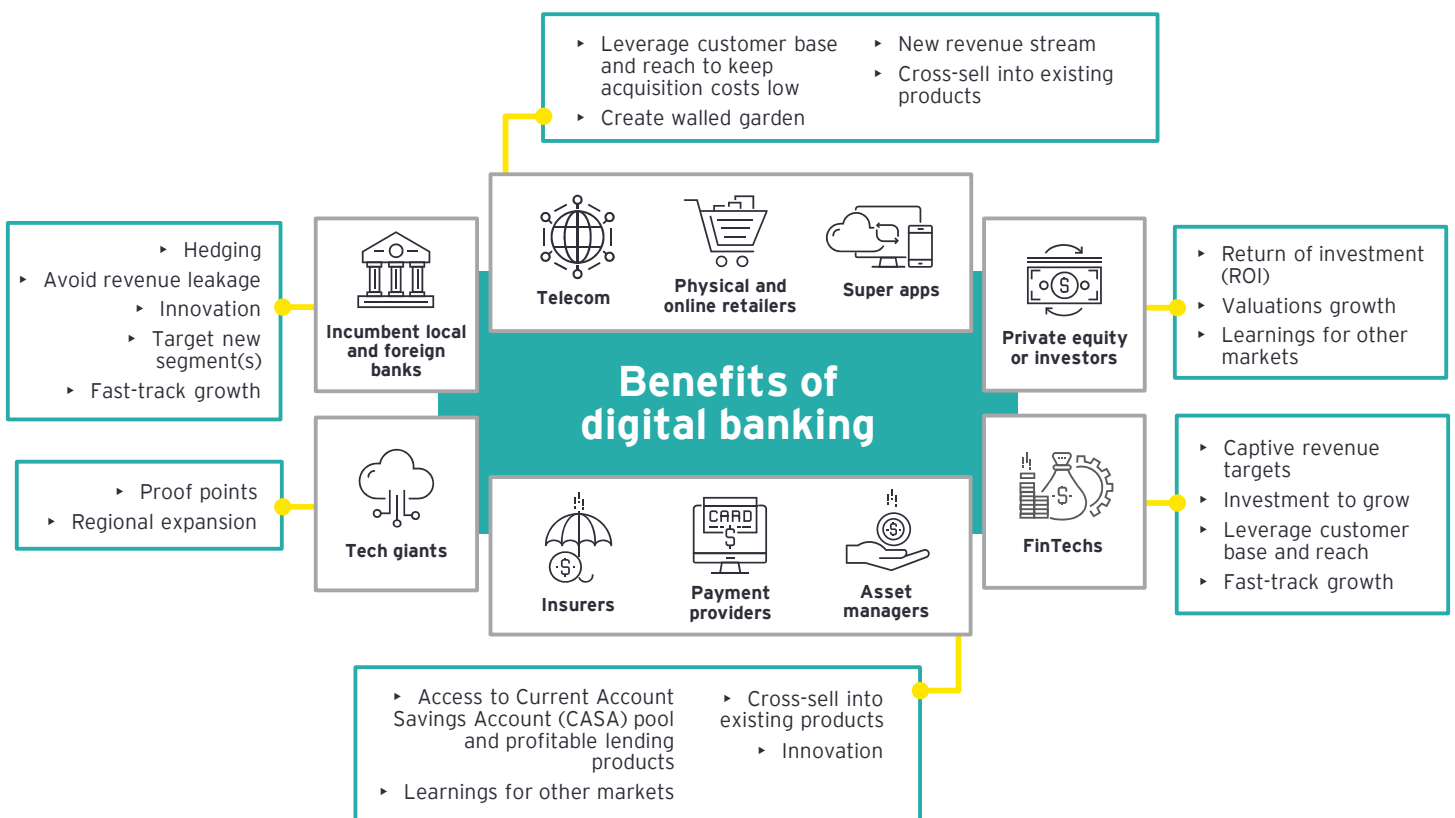


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Malaysia’s proposed digital banking framework **redefines the financial services ecosystem** and offers exciting opportunities for banking incumbents and new players to provide **responsible usage of suitable and affordable** financial services.
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Shankar Kanabiran
Partner and Deputy Consulting Leader
Ernst & Young Advisory Services Sdn Bhd

The case for digital banking participation

Players across different industries can benefit in unique ways:

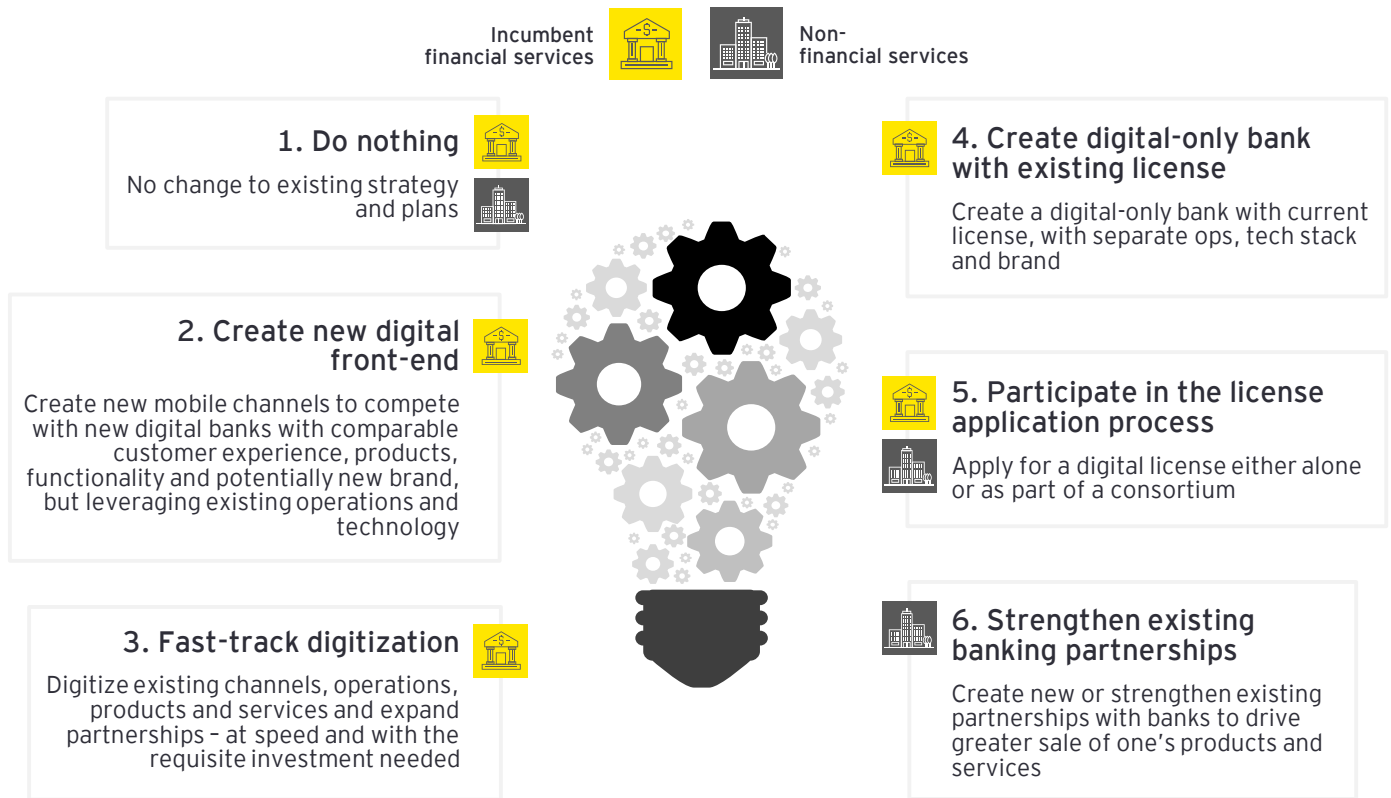


Sources:
▶ EY Consulting

Your digital transformation collaborator

How can EY teams help?

In response to the digital banking regulations in Malaysia, both incumbent financial services institutions and non-financial services institutions can explore a number of options:



EY teams can help you from strategy to execution in your digital bank journey, from assessing your strategic options and partnerships to all aspects of the application submission process for setting up a new digital bank.

Illustration: An Asia-Pacific digital bank

EY professionals advised a digital-only bank on its strategy and implementation.

Metrics achieved:

Performance

- ▶ Acquired 1m customers within 5 days (currently 10m)
- ▶ Breakeven within 3 years

Customer

- ▶ Majority of customers aged 30-80
- ▶ 80% of bank accounts are active

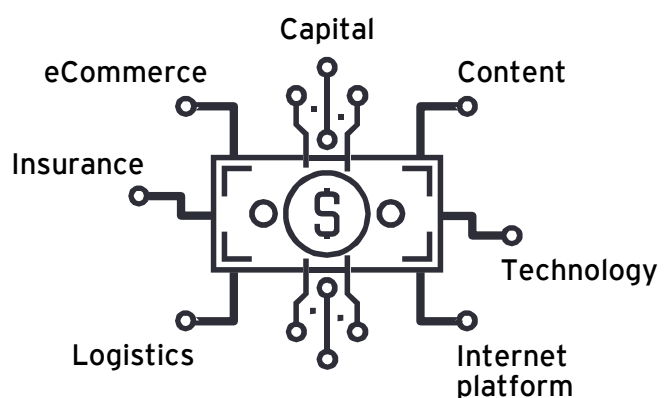
Products

- ▶ Account opening < 7 mins
- ▶ Unsecured loan < 1 min

Operations

- ▶ Cost-to-income ratio lower than bank average
- ▶ 1/3 of workforce are IT specialists

Key industry partners



Sources:
▶ EY Consulting

EY contacts



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